The Globalization of the Crisis in American Economic Education
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# The Globalization of the Crisis in American Economic Education

Alice H. Amsden

Professor Coats has done an excellent job in conveying the severity of the crisis consuming American economic education. ". . . American economics," he writes, "is currently in the grip of a narrowly technocratic species of professionalism that is failing to fulfill the reasonable aspirations of many of its members . . ." (Coats 1992, 348). He lends historical perspective to this myopia by noting that a thoughful, earlier study on American economics, by Howard R. Bowen, observed a similar tendency among academics—to burrow into their own theories without bothering much about grounding them in empirical reality.

Between 1953, the year of the earlier study, and 1991, the year of the recent economic education report, two simultaneous but opposing developments suggested the possibility that the weaknesses of American economic education were making a difference. On the one hand, free-market theory was triumphing both intellectually and politically within the profession and in Washington. On the other hand, the two countries closest to the free-market ideal, Great Britain and the United States, were showing the most alarming evidence of economic decline, whereas Eastern Asia and Western Europe, much further away from the textbook model, were growing the fastest.

Most discussion of the negative consequences of American training of Ph.D. economists concentrate on the United States. In this comment, I want to suggest that the ill effects are global in impact, diffused by international organizations and by the large number of economists from developing countries with American degrees.

The fast-growing East Asian countries have generally represented an embarrassment to American economists. Some have dealt with this by arguing that, if Japan and its neighbors had followed free-market theory, they would have grown even faster. This argument, however, tends to be doctrinal because no convincing proof can be provided in its defense. More typically, economists have merely ignored the intellectual challenge of an alternative economic development paradigm. As James Fallows (1991, 7) observed, "Very few examples from Japanese (or Korean) industrialization can be found in American textbooks, since they don't fit the theories that the books contain."

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In my own research on East Asia, I found that not only did government not "get the prices right," it deliberately had to get them "wrong" if industrialization was to germinate (Amsden 1989). In the 1960s, despite the fact that South Korea and Taiwan had some of the lowest wage rates in the world and possibly the best human and physical infrastructure among developing countries, and despite the fact that they repeatedly devalued their exchange rate to satisfy American aid advisors, they still could not compete either at home or abroad on the basis of market-determined production costs against Japan, which had better quality products and lower unit labor costs because of higher productivity. Neither South Korea nor Taiwan were competitive on the basis of market-determined production costs even in a leading, labor-intensive sector like cotton textiles, where one would have anticipated both countries to have a comparative advantage. The Korean and Taiwan governments, therefore, had to intervene with subsidies in order to trigger industrial development.

East Asian capital markets from the 1960s through the 1980s provide evidence of the wrong prices. South Korea, for example, had a three-tier capital market, with a competitive real interest rate (ranging from 40 percent to 20 percent) most closely approximated in the "curb" market, which was largely outside government control. By contrast, the real interest rate of state-owned commercial banks, which was charged to firms in targeted industries, was barely positive. The real interest rate on borrowed foreign capital, which the government controlled and allocated to its most favored firms, tended to be negative because of inflation and a fixed exchange rate. All three interest rates, operating side-by-side, could not have been right. The negative real price of foreign long-term investment capital was fundamentally wrong in a capital-scarce country.

The reason why South Korea and Taiwan grew faster than other late industrializers is not because they bowed deeper at the altar of free markets but because they allocated subsidies according to a different principle. In slower-growing late-industrializing countries, subsidies have tended to be allocated according to the principle of giveaway. In East Asia, they have tended to be allocated according to the principle of reciprocity, in exchange for concrete performance standards with respect to exports, output, training, and research and development. In all late-industrializing countries, labor has tended to be sternly disciplined by the state, but in East Asia, capital has also tended to be disciplined. Such discipline in South Korea insured that a big state-orchestrated push into heavy industry paid off handsomely in the form of high growth rates of output and exports.

East Asia's unorthodox economic practices have generally elicited a response of denial and downplay among the American-trained economists who occupy leadership roles in the Bretton Woods institutions—the World Bank and International Monetary Fund. A controversial report prepared by the World Bank's own independent evaluation arm said as much. Bank economists were faulted for having interpreted East Asian success largely in terms of market incentives, with little regard for the importance of institu-

**TABLE 1**
**The Number of American-Trained South Korean Economists, 1970–1990**

| Year | A-TKE |
|---|---|
| 1970–1979 | 204 |
| 1980–1989 | 466 |
| 1990 | 131 |
| Total | 801 |

*Source:* Computed from *Dissertation Abstracts International*, Ann Arbor, Mich., University Microfilms International.

tions and industrial policy (World Bank 1992). This misleading message continues to be conveyed to other developing countries.

As the influence of the Bretton Woods institutions and other international aid-related organizations spread after the 1960s, it became indispensable for career-minded economists in developing countries to obtain an American Ph.D., thereby shoring up the revenues of U.S. graduate schools. In the case of Korea, American-trained Korean economists (A-TKEs for short) numbered as many as 801 between 1970 and 1990 (compared with only 305 for Japan, whose population is roughly three times larger). As indicated in Table 1, a bunching of A-TKEs occurred after 1980, when free-market economics became more entrenched in American classrooms and demands from Washington that developing economies privatize, liberalize, and deregulate became more insistent.

Foreign economists holding American Ph.D.s, however, did not always aid development because their training lacked an appreciation of the importance of institutions in constraining the outcome of policy choices. American-trained Korean economists were the champions of a financial liberalization to increase equality and efficiency. In the presence of big business groups, however, financial liberalization led to more, not less, concentration of capital. The A-TKEs were allies of the World Bank in denouncing a government-led investment drive in heavy industry, although heavy industry supplanted light industry as a leading sector when Korean wage rates began to rise.

Coats's historical perspective on American economic education creates gloom about the possibilities for change. The worldliness of the American economics profession, however, is more than meets the eye. Most American economists may not incorporate the real world into their analyses, but when the political climate changes, the orientation of their work changes as well. A hopeful sign for change has come from the Japanese Delegation to the World Bank:

> Japanese officials said the Bank has put too much faith in "market mechanisms" in the past in its efforts to help the developing world and has placed excessive reliance on deregulation and liberalization.

> They called that approach "simple-minded" and said that it is based on outmoded Western concepts that fail to take account of the successful strategy pursued by Japan and some of its Asian neighbors in developing their economies. (Miller 1991, 1A)

Japan's outspokenness has put it at loggerheads with the bank's American delegation.

Thus, as the competitiveness of nations changes, and the Anglo-Saxon countries continue to lose ground, the economics profession may change after all, just as an industry that is no longer able to compete must ultimately restructure if it is to survive. In both cases, however, one may anticipate that the restructuring process will tend to be slower and more socially costly if it is the outcome of desperation rather than deliberate planning. Sadly, Coats leads us to believe that change in American economic education will follow the former route.

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